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Supreme Court, U.S.
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No. 00-1155

In the
Supreme Court of the United States

ROSEMARY C. BUTCHER, et al.,
Petitioners,

v.

JOBST W.F. BLACHY, et al.,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

PETITIONERS' REPLY BRIEF

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Petitioners reply to Respondents (all other parties, except the United States) as follows:

Argument 1. Where no indemnification has been provided by a seller which lacks title to real estate, a constructive trust against identifiable purchase moneys in the seller's possession could be appropriate, but not against the real property; where indemnification has been provided the "purchaser," there is no longer any relationship between the parties which would sustain a constructive trust action to recover the purchase money. The insured Respondents never had any interest in the real property or any fiduciary relationship with the owners.

Where an agreement of sale is not consummated, due to lack of title in the "seller," the "buyer's" sole remedy is an action at law for damages for breach of contract. Petition, page 25. Where the transaction is completed, and the purchase money has been paid over to the "seller," the putative "buyer" is certainly entitled to attempt to recover **his money in** law or in equity, where no indemnification has been provided. See page 10 of Respondent's Conditional Cross-Petition for Writ of Certiorari.

But, where indemnification, in the form of insurance, has been provided, or, where the "seller" has paid the money over to lien holders, any fiduciary relationship between the "seller" and "buyer" is at an end. There is no longer a monetary constructive trust claim because the seller has performed his agreement by providing for reimbursement of the purchase money. In *Nash v. New York Life Ins. Co,* 272 Mich 680 (1935), syllabus 4 reads:

> "Upon the occurrence of a loss under an insurance policy the contractual status between insured and insurer changes from a contingent

> liability on the part of the insurer to an absolute liability."

An insurer cannot agree with an insured to shift its liability to someone else, after a loss occurs. *Daiie v. Ayvazian,* 62 Mich App 94, 100 (1975); *Madar v. League General Ins Co,* 152 Mich App 734, 742 (1986). What is happening is that Lawyers Title and its insureds have supposedly agreed that they will, by this action, try to shift Lawyers Title's admitted liability to Rosemary. Lawyers Title has breached the third party beneficiary agreements entered into with the development corporations, to indemnify the insureds against monetary loss. *See* MCL 600.1405.

On Petition page 25, Petitioners pointed out that "the insured Plaintiffs parted with money, and, they are entitled to recover money from the insurer." Petitioners made the same argument to the lower courts. In their Response and in their Conditional Cross-Petition for Writ of Certiorari, Respondents advance two conflicting claims of entitlement.

In their Response to the Petition for Writ of Certiorari, page 4, Respondents argue:

> "The constructive trust is not a lien, but a judicial declaration that the Butchers never had a right to assert title **against the condominium owners**. Any "title" in the Butchers' names was in trust for the rightful owners, **from the day they were wronged**. Because the Butchers' acts were wrongful, they had no valid interest in the properties. The condominium owners did not hold a "lien" on the Butchers' title. They owned the property - bought and paid for. The Butchers had no lawful interest on which to impose a "lien." They owned nothing.

> The Butchers' **fraudulent title** was wrongfully withheld from the condominium owners **from the day LTDC, the Butcher company, conveyed to them**. (Emphasis Supplied).

Under this argument, Respondents concede Alexander and Rosemary acquired and held good title to the **17.83** acres from and after July 12, 1978. After all, they paid for the property with their own money; they owned the property, free and clear, on July 12, 1978; the property had not been committed to a recorded Master Deed as of July 12, 1978; and, no Respondent has made any claim against either spouse before October 22, 1981, the date of the first "sale" by LTDC.

In their Conditional Cross-Petition, Respondents argue:

> Page 3: "The Court of Appeals properly affirmed the district court's finding that the Butcher defendants held the subject property in constructive trust for the cross-petitioning condominium owners. That finding was based upon the Butchers' misleading and deceptive conduct that took place beginning in 1978. Beginning in 1981, the Butchers' companies conveyed the condominiums to the cross-petitioners." Citing, at Page 41, *Stephenson v. Golden,* 279 Mich 710, 746, 276 NW 849 (1937), and *Nichols v. Martin,* 277 Mich 305, 269 NW 183 (1936).

Nowhere do Respondents claim or attempt to show any interest in the property before October 22, 1981, or, any fiduciary relationship between the insured Plaintiffs and Petitioners, at any time relating to the real property. The

purchase agreements and the deeds to the insureds were admittedly void.

Stephenson involved a claim against a real estate broker who, while engaged as Plaintiff's agent, bought real property in his name, rather than in the name of his principal. *Nichols* similarly involved a claim of wrongful acquisition by a party occupying a fiduciary status. These cases are inapplicable because neither Alexander nor Rosemary had any fiduciary obligation on July 12, 1978, to any respondent. They acquired the 17.83 acres for their own purposes. There is not even a claim that any insured even knew the couple in 1978.

A void contract cannot create any legal or equitable rights in the parties. In *Scott v. Bush,* 26 Mich 418, 420 (1873), the Court stated:

> "We have held in ... that a contract void under the statute of frauds, is a mere nullity, and cannot be used for any purpose whatever. And we cannot conceive of such a thing as a contract which cannot be enforced as a contract, and yet can be the foundation of legal obligations arising out of nothing else."

Plaintiffs have no cause of action except for restitution from LTDC and/or HCDC. For more than 100 years, the law in Michigan has been that:

> "The contract set out, being void under the Statute of Frauds, cannot be used as the foundation of any legal or equitable right. If the party pays money under such a void contract he may recover it back in assumpsit, ..."

Kelly v. Kelly, 54 Mich 30, 48 (1884). *See also Thorbahn v. Walker' Estate*, 269 Mich 586 (1934).

Respondents' claim, then, is that the "conveyances," after September of 1981, by the development corporations to "purchasers" were wrongful because neither corporation had valid title, which "wrongful" acts gave immediate rise to a constructive trust over property owned by Alexander and Rosemary, by the entireties, even though neither spouse was a party to the "sales" transactions. Respondents now concede there was no "wrongful" conduct in the acquisition of the property by Alexander and Rosemary in 1978. They insist that even though the corporations provided full indemnification to the "purchasers" from them, covering the void deeds, the insureds somehow acquired an ownership interest in the real property because they paid the agreed "purchase" moneys to non-owners.

The lower courts never paused to consider why, if lack of marketable title by a seller gives rise to a constructive trust against property owned by another, this is the first case in the 224 year history of the country to so hold. The short answer is that the parties to a sales transaction are not in a principal/fiduciary relationship and, in any event, the purchaser sustains no injury where the agreed-upon indemnification is provided.

Moreover, the proposition that a person who owns or controls a corporation and who causes that corporation to hire and pay a title insurer for 100 or more record title examinations, as required by state law, is somehow acting "wrongfully," is absurd on its face. The only relevant or meaningful title representations to the "purchasers" were contained in the title insurance commitments, as required by law, which were prepared by the title insurer, which thereby

obligated itself to insure the title under the specified conditions. If a title insurer can go against the true owner, despite its mistakes, it can never have any liability under its policies.

In their Conditional Cross-Petition, Respondents, pages 8, 9, cite *In re: Omegas Group,* 16 F 3d 1443 (6th Cir 1994), and, then at page 13, ask the Court to overrule it.

Omegas involved a claim of entitlement, under 11 USC § 541(d), to a constructive trust over money paid by Plaintiff to the bankruptcy debtor shortly before the filing, because debtor "wrongfully" (page 1451) appropriated Plaintiff's money. The panel rejected Plaintiff's claim saying, page 1451:

> "We think that § 541(d) simply does not permit a claimant in the position of Datacomp to persuade the bankruptcy court to impose the remedy of constructive trust for alleged fraud committed against it by the debtor in the course of their business dealings, and thus to take ahead of all creditors, and indeed, ahead of the trustee.

In this case, where the sellers provided indemnification, the court awarded relief against a non-party to the business transaction which is a double recovery for respondents.

Pursuing the § 541 (d) argument further, Respondents cite from the Legislative history of the Section, at page 10:

> "Situations occasionally arise where property ostensibly belonging to the debtor will actually not be property of the debtor, but will be held in trust for another. For example, if the debtor has incurred medical bills that were covered by

> insurance, and the insurance company had sent the payment of the bills to the debtor before the debtor had paid the bill for which the payment was reimbursement, *the payment would actually be held in a constructive trust for the person whom the bill was owed."*
>
> The US Congress clearly intended that § 541(d) of the Bankruptcy Code would not encompass property a debtor holds subject to a constructive trust. This court's holding to the contrary in *Omegas* directly conflicts with Congress's intent." (Emphasis added by Respondents).

Whether *Omegas* was correctly or incorrectly decided, the observation pertinent to this suit is simply that, as in *Omegas,* there was never any pre-existing fiduciary relationship between the insureds and Alexander, or Rosemary.

When the corporation "sellers" acquired the insureds' purchase moneys, without being able to convey marketable title to them, a constructive trust claim arguably could arise as to those funds received by the developers from the "purchasers," which are identifiable and still in the possession of the development corporations. Two applications of the § 541 (d) legislative history suggest themselves:

1. If the purchase money for a unit was paid to the seller, which failed to pay off a lien of record, making seller's title unmarketable, the purchaser could seek a constructive trust over the purchase money which should have been paid to the lien holder.

2. If Lawyers Title had paid the policies proceeds to the "seller," for the "seller" to indemnify the purchaser, it could seek a constructive trust over those moneys remitted by it which were not paid by the "seller" to the "purchaser."

Following the money, to make oneself whole, could make some sense where that is the only possibility for recovery, but it makes no sense when indemnification has been provided. Lawyers Title is not entitled to recover on a subrogation theory because it has not paid the claims of its insureds, and, because, under Michigan law, it can acquire no right of subrogation by paying its own obligations. Any such payment is an extinguishment of the liability. *Michigan Hospital Service v. Sharpe,* 339 Mich 357 (1954).

A constructive trust could be claimed over the purchase moneys "wrongfully" obtained by the development corporations, but not over the real property.

Argument 2. Every Plaintiff had constructive notice of Alexander and Rosemary's title to the property. *McBride v. McBride,* 250 Mich 601,603 (1930), *Houseman v. Gerken,* 231 Mich 253, 255 (1925), **whether or not they actually checked the record,** *Dwight v. Tyler,* 49 Mich 614, 616 (1883), at the time of any purchase after July 14, 1978. Recording of a deed in Michigan is constructive notice to all. If Debtor and her spouse had wanted to conceal the conveyance of July 12, 1978, from LTDC to themselves, they would not have recorded the Deed.

Argument 3. Lawyers Title had actual knowledge of Alexander and Rosemary's title to the property before it made any title commitment or policy errors.

Respondents, pages 5, 6, and 7 of Response, acknowledge that Lawyers Title was advised by letter dated

August 17, 1978, as to the "state of the title up until July 13, 1978." This letter alerted Lawyers Title to the fact that record title changed after July 13, 1978. After being alerted to changes in the record title, Lawyers Title issued a sample commitment and a mortgage policy in August of 1978, items 8 and 11 of Respondents' App 2a, which correctly show LTDC to be the owner of record on July 13, 1978.

Argument 4. Respondents are attempting to bamboozle this Court.

To Petitioner's charge, Petition page 29, that there was no **erroneous** commitment issued in July of 1978 (as the 6th Circuit erroneously held, App A at 4a, based on Respondents' false representations to it), Respondents concede that there was no erroneous commitment, and, that Lawyers Title in fact issued an **accurate** sample commitment in August of 1978, "as of July 13, 1978," Response pages 5, 6, and 7. So, everything is all right, according to the Respondents. But, the only basis given by the 6th Circuit for imposing the constructive trust, as of 1978, was Respondents' false claim of an erroneous commitment attributable to Alexander's conduct in July of 1978. There was no erroneous title commitment issued in July or August of 1978. Alexander did not mislead Lawyers Title. In his letter of August 17, 1998, he specifically advised the examiner that record changes occurred after July 13, 1978. Respondents should not be rewarded for making false representations to the Court. See Argument 3, Ante.

Argument 5. Contrary to Respondent's claim, page 3 of Response, this action was barred by 11 USC § 362(c) on October 16, 1991, Petition page 27.

Respondent's Motion to Lift the Automatic Stay, as to Rosemary, dated August of 1991, was denied by the Bankruptcy Judge. The automatic stay was lifted as to

Rosemary, by Order of January 20, 1998. (No fraudulent conveyance count was ever filed). Respondents' First Amended Complaint paragraph 36 reads that Rosemary's bankruptcy prohibited Plaintiffs from adding her as a defendant in this action.

Respondents repeatedly claim that constructive trusts arose on the day(s) the insureds were "wronged," Response page 4; Conditional Cross-Petition, pages 3, 4, 5, 6, 7, 8, which claims, in every case, arose years before the commencement of Rosemary's bankruptcy case. 11 USC § 362(a)(1). Obviously, Respondents were trying to destroy Rosemary's prepetition right of survivorship in the 17.83 acres when suit was commenced on October 16, 1991. Even Respondents understood that the suit was barred, but they filed it anyway.

Argument 6. The decision of the 6th Circuit conflicts with decisions of the other Circuit Courts.

Respondents, page 1 of Response, say the decision does not conflict with decisions of other Circuit Courts, but they do not cite any other Circuit Court decision which purports to destroy the survivorship rights of both the debtor and his or her spouse, nor do they cite any other court decision which holds that entireties properties are divided into moieties where one spouse files a Chapter 7 Petition and claims the "state-law" exemptions.

CONCLUSION

The exemptions available under 11 U.S.C. § 522(b)(2)(B) cannot be ignored to permit such an incompetent insurer to avoid its liabilities.

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